19 October 2018

Mr. Oleksandr Dombrovskyi
Acting Head of the Fuel and Energy Sector
Committee of Verkhovna Rada of Ukraine

Subject: Draft Law on amendments to some laws of Ukraine to ensure competitive conditions of production of electric energy from alternative energy sources (registration No. 8449 dated 07.06.1018)

Dear Mr. Dombrovskyi,

Thank you for inviting the international donor community and international organisations to participate in the discussions on the Draft Law "On amendments to some laws of Ukraine to ensure competitive conditions of production of electric energy from alternative energy sources."

We would also like to express our appreciation for your personal engagement and taking the lead in the process of seeking consensus and adoption of a good quality law as soon as possible.

Renewable energy is an important area of the European Union's ("EU") cooperation with Ukraine in the framework of the Association Agreement and the Memorandum of Understanding on Strategic Energy Partnership. It is also a very strong and a growing focus area of the policy dialogue and investments of the International Financial Institutions. Support of the Energy Community Secretariat to Ukraine on compliance with the Energy Community *acquis* also plays an essential role in the energy sector reform process in Ukraine.

We strongly support the need to shift from the existing Feed-in-Tariff called Green Tariff in Ukrainian legislation ("GT") regime to a competitive auction-based system. Those of us who are financiers, including the European Bank for Reconstruction and Development ("EBRD") and the International Finance Corporation ("IFC"), believe that the current system – while helpful in launching the sector – is no longer appropriate to support its long-term development. As a result, the EBRD will no longer be able to finance new projects in Ukraine that are relying on the GT other than those already in its pipeline, unless the amended law is approved to guarantee the long-

term economic sustainability of the sector, thus providing the necessary comfort to investors and financiers.

We are aware that the committee and other stakeholders are discussing certain issues related to the amended law. We would therefore like to share below the common position of the European Commission ("EC"), Energy Community Secretariat ("EnCS"), the EBRD, the World Bank ("WB") and the IFC on the main elements of the amended law that were raised and have been discussed with all the relevant stakeholders of the working groups established under the lead of the Energy Committee of the Verkhovna Rada.

1. The renewable auctioning support scheme should come into force as soon as the amended legislation becomes effective;
2. We do not support any extension of the GT for all technologies;
3. We propose to introduce the maximum possible duration for the new support mechanism to generate the most affordable electricity for both the consumer and the country;
4. We do not support regional quotas to ensure the process is efficient, competitive and transparent;
5. The ministry of Energy and Coal Industry must publish long-term renewable development targets and annual and 5-year quota forecasts to provide the necessary long-term visibility to investors;
6. A cost efficient, transparent and technically-compliant electronic platform should be used to support the auction process;
7. A ratio of award to demand should not be higher than 0.8 to guarantee the competitiveness of the process;
8. The required bank guarantees to be able to participate to the auction process should be of at least EUR15,000 per MW of installed capacity in order to deter speculative or frivolous bids;
9. We recommend that the balancing obligations are consistently set for auctioning process with a pre-condition of a liquid intra-day market being in place for start of the full balancing responsibility of renewables.

Our common position on the more detailed provisions of the amended law are presented as an annex to this letter.

We urge the Ukrainian authorities to pass the new law as soon as possible in line with the comments and suggestions made in the annex to avoid a loss of momentum and potential fall in investment in the sector if the introduction of auctions is delayed.

We would also like to confirm our interest and readiness to continue our engagement and to support the Energy Committee in its work.

Yours sincerely,

Torsten Woellert, Team Leader
Energy, European Commission

Janez Kopac, Director
Energy Community Secretariat

Francis Malige, Managing Director, Eastern Europe and the Caucasus
European Bank for Reconstruction and Development

Jason Brett Pellmar, Regional Manager for Ukraine, Belarus and Moldova
International Finance Corporation

Satu Kähkönen, Country Director for Belarus, Moldova and Ukraine
World Bank

Enclosed: EnCS, EU, EBRD, World Bank, and IFC comments on key element of the draft law No 8449 of 07.06.2018.

cc:

Mr. Volodymyr Groysman, Prime Minister, The Government of Ukraine
Mr. Andriy Parubiy, Chairman of the Verkhovna Rada

	Issues	EnCS / EU / EBRD / IFC / World Bank Comments – 19.10.18
1	**Date of introduction of new support system**	We believe that the new support scheme should come into force as quickly as possible, with auctions introduced immediately following the entry into force of the amendments to the law. The first auction should be awarded no later than 31 December 2019, in order to allow for a transition period to ensure that all projects sufficiently advanced (see below) can still benefit from the tariff they were designed under.
2	**Deadline for signature of pre-PPA for completion of launched RES projects at feed-in tariff**	We believe that a 1 July 2019 cut-off to qualify for launching projects under the existing Green Tariff is reasonable, provided that the requirement to have a pre-PPA in place be complemented by more stringent criteria, such as having a grid connection and land secured in place.
3	**Pilot auctions**	We believe that it is very important to separate the concepts of pilot auctions from the Chornobyl Exclusion Zone project, which has very specific characteristics and will not be replicable under the wider auction scheme. The criteria should be clarified to note that 100 MW will be the aggregate capacity for each pilot auction. For the Chornobyl Exclusion Zone project and off-shore wind projects location-specific tenders should be conducted.
4	**Frequency of auctions**	We agree and recommend that the date of the first auction be specified as 1 October 2019. Auction frequencies twice a year appear to be reasonable.
5	**Mandatory participation in auctions**	Levels of 5 MW or 10 MW for solar and wind, respectively (declining to 1 and 3 in 2023) appear to be too high and constitute a risk of overcompensation, negative impact on competition and distortive effect to the transition of new projects to competitive bidding scheme. In any case, an assessment by the Anti-Monopoly Committee is an essential requirement to confirm the compliance of the scheme with the state aid obligations of Ukraine.. In the EU market, thresholds below which competitive bidding processes do not need to be employed are set at the level of less than 1 MW for solar or 6 MW generation units for wind. In order to address potential circumvention risks of this requirement setting aggregated capacity limits for the generation units of different RES technologies should be considered (i.e. an aggregated capacity limit for onshore wind generation units, an aggregate capacity limit for solar PV units, etc).
6	**Eligibility for participation in auctions**	The mandatory participation of all types of renewable energy producers above a specific threshold is reasonable.

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7	**Feed-in tariff**	We agree that the current scheme should remain unchanged through 1 January 2030 apart from the Green Tariff reduction, discussed below. Any extension would require a further reduction in the Green Tariff Rate, it would be complicated to implement and could alarm investors in the current uncertain and unstable Ukrainian investment environment.
8	**Reduction of feed-in tariffs**	The proposal to reduce the 2020 FiT by 30% for solar and 15% for wind appears to be reasonable. It is more likely to correctly reflect current and expected cost reductions.
9	**Revision of feed-in tariffs for biomass**	We do not object to the proposal to extend the current biomass FiT through the life of the Green Tariff, but not beyond 2030. We note, however, that a transparent and detailed analysis of other social, legal, economic and technology, investment cost factors needs to be carried out and discussed with stakeholders first. A separate legislative initiative could be more appropriate not to lose the focus on introduction of competitive bidding.
10	**Duration of support for winner of auction**	We support the proposal to extend the support duration for the winners of auctions to 20 years from the date of the plant's technical commissioning, which will provide: 1) a greater incentive and regulatory stability to investors; 2) a provide more affordable renewable electricity price for Ukraine.
11	**Quotas – who defines and approves**	We do not object the following proposal: The country-wide public support quota shall be established by the Cabinet of Ministers of Ukraine annually upon a submission from MinEnergo. The submission of MinEnergo should support reaching the mid-and long term renewables goal. Moreover, drawing on the inputs of relevant stakeholders such as the transmission system operator, the submissions should reflect factors such as the capacity of the grid to absorb RES, and measures adopted, implemented and envisaged to increase the capacity of the grid and flexibility of the electricity system. MinEnergo shall prepare, within 6 months of this law coming into force and annually thereafter, a report that: (1) identifies the volume of renewable energy generating capacity required to meet the target for such capacity set out in the Government's energy strategy; (2) establishes and justifies indicative quotas for the volume of capacity to be auctioned for support in each of the next five years. Upon approval of the Cabinet of Ministers this report shall be published.

12	**Principles for quota definition**	1. We do not support the introduction of regional quotas if technology specific auctions are foreseen and if the auction bidders are required to secure grid capacity prior to bidding. We also do not support quotas set by administrative regions. However, the law should explicitly allow location-specific auctions for the Chornobyl Exclusion Zone project and off-shore wind projects. Such auctions of pre-selected sites will have separate procedures. 2. We can agree with the proposal to introduce technology-specific quotas provided that no regional quotas are set and pre-qualification criteria include connection permit and secured land. With the little evidence in place, we do not support the proposal to allocate certain limit of each annual quota (20-25% of each annual quota to non-wind or non-solar technologies) at the level of primary legislation. Instead we recommend that in case if a specific allocation is made, it should be made by the Cabinet of Ministers and it should be required to be justified by considerations of grid stability, market and energy sources diversity and cost. Because renewable energy and power storage technologies and their costs are evolving very rapidly, mentioning a technological mix in primary legislation may lead to suboptimal results in several years; and changing primary legislation is a lengthy process. 3. Reservation of a 40% share of quota allocations for projects smaller than 50 MW could be too high in view of importance of reaching the necessary scale for market development and cost reduction vis-à-vis support for distributed generation and smaller scale projects. 4. To avoid speculative behaviour and reduce the risk of auction failure, we suggest to consider a restriction not allowing to increase annual quotas by transferring the non-awarded-quota/ not signed contracts to the following year. 5. Award should be non-transferable either to another company or to another final beneficiary (via selling the company awarded) prior to the project being commissioned unless the acquiring entity can demonstrate (i) the same legal, technical and financial capabilities and (ii) the maximum 25% share of the annual quota in the relevant by a single ultimate beneficiary in a given auction is not breached following the proposed acquisition.

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13	**Planning of quotas**	We recommend that MinEnergo have an ongoing obligation to publish an annual statement (1) stating the progress achieved towards the long-term RE goal, (2) the then current trajectory expected to reach that goal, (3) a list of supported projects and their implementation status, and (4), a timetable for auctions (including identifying volumes and technologies) for the coming 3-5 years.
14	**Who approves auction procedure**	Approval by the Cabinet of Ministers appears reasonable, with due consideration of the assessment of the Anti-Monopoly Committee of Ukraine.
15	**Auction`s customer**	We believe that having the Guaranteed Buyer as the auction's customer is reasonable.
16	**Auction platform**	We believe that a trusted, cost efficient and technically-compliant platform fulfilling the highest transparency, objectivity and fraud resilience standards should be used for the future auction system and that a specific platform should not be identified in primary legislation. The most important requirements for an auctioning platform should therefore be set in the primary law. (During the discussions of the working groups in Rada it was clarified that the ProZorro system is adaptable to renewable energy support auctioning requirements, and it can be set-up and be fully functioning within the shortest period of time. Its mandatory use for public procurement is set out in primary law (Law "On procurement"), fulfils the above requirements and has passed the test of practical use in Ukraine).
17	**Model of auction (design)**	An auction design relying on pay-as-bid (one-stage static auctions, with simultaneous openings of technical and price bids) appears to be reasonable.
18	**Competition at auction in case of limited interest**	A reduction in quota levels during auctions should be employed, and we suggest that the ratio of awards to demand not to be higher than 0.8.
19	**Max price of auction**	We suggest that each auction has the flexibility to set an objectively justified maximum price and to decide if that price will be published. If the maximum price is set at the Green level and disclosed, it may result in final auction prices at the level of the disclosed maximum price. However, the maximum price set for any auction should not be allowed to exceed the Green Tariff level.
20	**Measures to avoid concentration at RES market**	Limiting the maximum share of each annual quota to 25% for a single participant appears reasonable. We suggest that this be coordinated with the Antimonopoly Committee of Ukraine, and that all bidders in an auction be required to disclose their ultimate beneficial owners. It should be clarified that "single participant" means the ultimate beneficial owner.

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21	**Bank guarantee**	The level of the bank guarantee should be set at a per MW basis in order to deter speculative or frivolous bids. We recommend that the level be set at a minimum of EUR 15,000 per MW of capacity.
		We believe that certain basic technical requirements need to be fulfilled for a bid to be accepted, including: 1. grid connection secured; 2. initial environmental and zoning permission; 3. lease, ownership or option over land; and 4. minimum legal and technical criteria.
22	**Agreement structure**	There will be more than one agreement in existence, depending on whether the auction occurred in the period prior to the establishment of a liquid day-ahead market or after. Market participants awarded a purchase/sale agreement in the period prior to the establishment of a competitive and liquid day ahead market should be allowed to keep their initial contract (purchase/sale agreement) for the full duration of the support period. Market participants awarded support in the period after the establishment of a competitive and liquid day-ahead market will be granted a contract-for-difference, and will be selling power to the electricity market (which may include sales through one or more contracts). It should be made clear that participants already awarded a purchase/sale agreement will not be required to re-sign contracts-for-difference once the liquid day-ahead market has been established. In addition, we recommend that the law specifies the entity that will be responsible for determining that a **competitive** and **liquid** day-ahead market exists. The Anti-Monopoly Committee should be responsible for determination of existence of a sufficiently competitive market. The Regulator should be responsible for determination of existence of a liquid day-ahead market. Moreover, the law should specify the need for the criteria to be developed by which the competitiveness and liquidity of the market will be assessed (these criteria can include volume of trading, market churn, number of participants, their shares in the market etc).
23	**Simplified procedure for feed in tariff (same as for households) for economic entities**	We believe that a threshold of 150 kW appears reasonable. It should clarified in the law that for receiving the Green Tariff the same procedure and the same type of contract is given as in case of households.
24	**LCP top-up to auction price**	A clear, transparent and long-term process for planning the quotas and for granting the projects is the most effective measure to support local economic development and jobs. We strongly recommend against any

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		proposed local content preferences as this in contradiction to WTO rules and likely to lead to distortion of competition in auctions as well as to economic inefficiency and unnecessarily high cost of power. Due to declining costs of renewable energy technologies, the added value of renewable energy projects as well as the creation of jobs continues to shift from the technology components to the operation and maintenance of renewable energy projects. Typically above 80% of jobs are in operation or maintenance. Experience also shows that such policies have had an adverse impact in the long-run for a number of reasons: 1) rules have been challenged under the WTO, creating uncertainty for project developers, 2) it limits the number of market players and therefore competition, 3) foreign companies might open local plants, but this does not directly lead to profits for local companies, and 4) it can lead to higher levelised costs of energy supply.

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25	**Responsibility for imbalances**	We recommend that the balancing obligations are consistently set for auctioning process with a pre-condition of a liquid intra-day market being in place for start of the full balancing responsibility of renewables. Given the uncertainty around the future cost of balancing we also support the introduction of a reasonable cap for future participants to the auctions for the whole duration of their 20-year support to give them the necessary visibility to be able to invest. Separately from the Law, the capacity of key institutions involved in balancing can enhanced by sharing the experience of EU Member States how to minimize the risks and costs for the grid operators and the Guaranteed Buyer. We recommend that the Regulator's decision criteria be public and based on clear metrics such as trading volumes over the last twelve months, number and structure of participants, their shares in market segments, price volatility, etc. We recommend that the existing provisions allowing the aggregation of individual RES producers' balancing responsibilities by the Guaranteed Buyer be maintained. The potentially large untapped potential for increasing the flexibility of the whole system (not only on the infrastructure and renewable producers' side) along the supply and demand of the city system chain should be also analysed and used.
26	**Possibility for RES generators to sell directly at electricity market**	Market participants awarded support in the period after the establishment of a competitive and liquid day-ahead market will be granted a contract-for-difference, and will be selling power to the electricity market (which may include sales through one or more contracts).
27	**Settling the issue with limited duration of technical conditions for connection**	Relying on provisions identical to draft law 6081 (technical conditions apply during 5 years as of the date of granting) appear reasonable. Cancellation of connection permits not used is an important element for freeing-up available but unused grid capacity (in addition to grid investments and electricity system flexibility increase along the supply – demand chain).

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28	**ADDITIONAL**	Specify the time from auction award by which project must reach commercial operations and the physical start of production, for example 18 months for solar and 36 months for wind.